USING CREDIT to finance FARMHOUSE IMPROVEMENTS

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THIS PUBLICATION is written for extension agents, teachers, and others who work with farm families. It presents factual information concerning credit sources available to farm families for financing farmhouse improvements and lists some questions for families to consider in planning for credit. Some of the suggestions are equally important to the families that are paying cash for their housing improvements.

The facts and recommended procedures set forth here apply generally. Some of them may not be applicable in all localities. In such cases it will be advisable to get advice from local people.

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Many farm families have made progress in improving their houses in recent years. They have put in electricity, and are installing running water and modern waste-disposal facilities and central heating systems. Some families are planning to modernize their houses in other ways. They want to add insulation, build new cupboards in the kitchen, relocate the stairway, lay new floors, or add a utility room, an extra bedroom, or a porch. Other families are planning to build new houses.

These housing improvements will be financed in a variety of ways. Some families will cash their war bonds and use other savings. Others will pay for improvements out of current income. Still others will finance them with borrowed funds.

Information in this publication is concerned primarily with the last group, the families that are planning to use credit or are considering its use.

These people want to know: Is credit available for home improvements? What interest rate is charged? What, in addition to interest rate, should be considered in selecting a source of credit? Should improvements be made now or later when the farm is all paid for? How much should farm families invest in housing? These questions and other considerations are discussed in the pages that follow.

SHOPPING FOR CREDIT

Families seeking credit for housing improvements usually find it a good idea first to make a list of the credit terms that best meet their needs, and then to shop among the various places where they might borrow.

Credit Terms Favored by Families

The following are credit terms advantageous to families:

- Interest and other charges kept at a minimum.
- An amortized plan for repayment of the debt, with the repayment schedule fitted to the periods when the family receives its income—that is, annually, semiannually, quarterly, or monthly.
- Length of term such that annual payment of interest and regular installments on principal can be paid out of expected income.
- A loan contract that includes the following provisions:
  - Permits the borrower to repay the debt in advance of the due date without paying a penalty.
  - Permits the borrower to make extra payments on the principal in years of high income to offset lower payments in years of low income. Contracts with this feature are known as variable-payment contracts.

Sources of Credit

In considering the use of credit for housing improvements there are a variety of credit sources that families may wish to investigate. The two main sources are private lenders and agencies sponsored by the Government.[1]

Private lenders

Owner-operator farm families that can get credit from commercial lending institutions for running the farm business usually are able to obtain loans for repairing and improving their houses from the same sources and at the same rates. The local bank is the agency most often patronized. Others include mortgage companies, insurance companies, building and loan associations, and personal finance companies.

A family with a good credit rating usually can obtain a loan of not more than \$300–\$500, to be repaid within a 12- to 18-month period, on the security of a promissory note. Families obtaining cash loans of \$1,000 or more usually give a mortgage on their farms as security for the debt. The length of term of such a loan depends upon several factors, among which are the legal restrictions under which the bank operates and the plan for repaying the principal sum. For example, national banks may make unamortized loans up to 50 percent of the appraised value of the real estate for terms up to 5 years. The amounts may be increased to 60 percent and the terms to 10 years if 40 percent of the principal is amortized during the 10-year period. These restrictions are waived for insured mortgage loans.

Farm families often can obtain long-term loans from a neighbor or other person who has money to lend, perhaps from a relative or a retired farmer who lives on the adjoining farm. These loans may run for a few years only or for a longer period. The lender may take a mortgage on the farm of the borrower as security, or he may require no other security than the borrower's personal note.

[1] Information on credit sources applies to conditions as of 1949. These vary in different localities and laws and regulations may be changed.

Some farm families also obtain short-term loans from individuals. The interest rate and other terms are those mutually agreed upon by borrower and lender. In either case, the arrangements usually provide for the payment of interest annually or semiannually and payment of the principal at the end of a specified period. Only occasionally does such an agreement provide for repaying the principal in annual or semiannual installments.

Merchant credit is another source drawn on by farm families. "Merchants" include lumber and millwork dealers, building supply companies, hardware stores, department stores, and mail-order houses. Dealers who install equipment, such as plumbing, sometimes arrange credit for their services as well as for the merchandise. Merchant credit may be the open-book credit, commonly known as charge accounts, or installment credit.

Charge accounts are in quite general use among families that are using considerable amounts of lumber, millwork, hardware, and plumbing equipment in their home-improvement programs. In some areas retailers bill their customers for payment at the end of 60 or 90 days and allow a discount of 1½ or 2 percent to customers who pay the bills when due. Other retailers charge interest on accounts that are unpaid at the end of a specified time, such as 30 or 60 days.

Installment credit frequently is used by farm families that are modernizing their houses and are purchasing expensive durable articles such as refrigerators, ranges, and plumbing equipment. Retailers extending this type of consumer credit may require a down payment up to one-third of the cash price. The contract usually calls for paying the balance (which includes the carrying charge) in equal monthly installments extending over a period of several months. Usually the seller retains title to the article until the payments are completed. Under the contract he can take the article back if payment is not made.

The size of the carrying charge varies greatly, depending on such considerations as the type of article sold, the amount of the sale, the second-hand value of the article, and the length of the period over which the dealer's money is outstanding. Goods purchased on the installment plan may cost 10 to 40 percent more than if bought for cash.

Agencies sponsored by the Government

Three Government-sponsored lending agencies make loans to farm families for housing improvement, provided the families can qualify for the credit. They are the Farm Credit Administration, the Farmers Home Administration, and the Rural Electrification Administration.

Farm Credit Administration.—Federal Land Banks and the Production Credit Associations, both units of the Farm Credit Administration, make loans for housing improvements. The Cooperative National Farm Loan Associations provide long-term loans from the Federal land banks for buildings or other structural improvements to farm property. Loans to member-borrowers may be made up to 65 percent of the normal agricultural value of the farm. These loans, running from 5 to 34 years, are now made at 4 percent interest except in a few States where the rate is 4½ percent. A mortgage on the farm is given as security for the debt. These loans are repaid on the amortized plan.

Production Credit Associations make loans to their member-borrowers to finance housing improvements and to pay for costlier items of household equipment. At the time the member-borrower is borrowing money for house improvements he probably is also getting a production loan for operating his farm. If so, the promissory note will cover both loans, and a chattel mortgage on the livestock, farm machinery, or crop will be given as security for the entire debt.

Usually the terms of a Production Credit Association loan call for repayment or material reduction in the amount due on the face of the note within a 12-month period. The interest rate usually charged is 5 to 5½ percent, depending upon the Production Credit Association district in which the family lives. Usually borrowers make and repay these loans on a budgeted plan.

Farmers Home Administration.—The Farmers Home Administration serves farm families that are unable to obtain needed financial assistance from other credit sources on reasonable terms. An Act of Congress established the agency in 1946 and at the same time abolished the Farm Security Administration, and the Emergency Crop and Feed Loan Division of the Farm Credit Administration. The act transferred the assets and liabilities of the latter two agencies to the Farmers Home Administration

Real estate mortgage loans are made by the Farmers Home Administration to: (1) Owners of farms smaller than family-type units or farms inadequate in other ways, in order to enlarge, develop, or improve the farms; (2) veterans with agricultural experience, farm tenants, farm laborers, and share croppers so that they may buy family-type farms and improve the land and buildings. Such loans may, and often do, include funds for house improvements.

The Farmers Home Administration also is authorized to make loans to disabled veterans to enable them to purchase farms that are smaller than family-type units. Since these veterans have a pension, they are not wholly dependent on the income from the farm to meet expenses for family living and farm operation, to finance improvements on the buildings, and to repay their loans.

Loans made for all of the purposes mentioned above are long-term loans, secured by a mortgage on the farm. The family pays 4 percent interest on these loans. The repayment schedule provides for amortization on a variable-payment plan over

periods up to 40 years. Families are encouraged to repay their debt in less time.

In addition to these long-term loans, the Farmers Home Administration also extends short-term credit to farm families unable to obtain loans on the usual commercial terms. Some of this credit may be used for housing improvements.[2]

Rural Electrification Administration.—The Rural Electrification Administration provides credit to help rural families attain the full benefits of electricity with minimum delay. The REA lends money for this purpose to rural electric cooperatives that it has financed, and they in turn lend the money to their members.

Operators of these electric systems make consumer facilities loans, as they are called, to farm families to help finance the wiring of the farmstead, the purchase and installation of a pump and plumbing, and the purchase of electrical equipment and appliances for the home and the farm. The borrowing family is urged to make a 20-percent down payment although a minimum of 10 percent is permitted. Credit is extended to the family for the balance of the cost of the improvement up to a maximum of $500 for a single loan.

The farm family usually pays 4 percent interest on these loans. They are repaid on an amortized plan. The principal must be repaid within five years or within a shorter time if required by regulations of the Federal Reserve System. Up to February 28, 1949, the Rural Electrification Administration had approved $13,918,588 in consumer facilities loans to farm families, which is about 1 percent of the total loans it had approved.

Insured Loans and Guaranteed Loans

Insured loans often are more readily available for financing housing improvements than loans that are not insured. With the protection of credit insurance or a Government guarantee the lending agency may be able to make a larger loan to the family and for a longer period than it could make otherwise.

The Federal Housing Administration insures a limited volume of loans, particularly short-term loans, to farm families for the modernization and repair of houses. Under the terms of the short-term loans applicable to farmers the maximum amount that can be loaned to any one borrower is $2,500 and the maximum maturity date is 3 years and 32 days. At present, the maximum financing charge for a modernization loan is $5 per $100 for each year of the term of the loan. The loan is discounted; that is, the charges are deducted in advance. The family that applies for and obtains a $100 loan for 1 year actually receives $95. The terms provide for repayment of such a loan in equal monthly installments. The maximum charge paid by the borrower (which includes an insurance premium of ¾ of 1 percent per annum of the net proceeds to the borrower) is equivalent to somewhat less than 10 percent per year on the average outstanding balance.

The Farmers Home Administration is authorized to insure farm-mortgage loans made by private lending agencies and individuals to farm families that can qualify. These insured mortgage loans are limited to 90 percent of the "reasonable value of the farm and necessary repairs and improvements thereon." This includes repairs and improvements on the dwelling. Insured loan borrowers pay 3 percent interest plus a 1 percent annual mortgage insurance charge.

Under Title III of the Servicemen's Readjustment Act of 1944 (the "GI bill") veterans of World War II who wish to obtain loans for the purchase of farms and the construction or improvement of farm buildings, including houses, are enabled to do so. Any loan obtained by a veteran from a lender for any of the purposes specified in Title III may be "guaranteed by the Government by this title in an amount not exceeding fifty per centum of the loan: *Provided*, That the aggregate amount guaranteed shall not exceed $2,000 in the case of non-real-estate loans, nor $4,000 in the case of real-estate loans." The Veterans' Administration is the agency authorized by the Government to administer this program.

Thus, if a veteran wants to borrow $10,000 to buy a farm and install modern facilities in the house, the Veterans' Administration is authorized to guarantee the loan up to $4,000. The guarantee is made to financial institutions such as banks, savings and loan associations, and insurance companies, and also to individuals, to encourage them to make loans to veterans on favorable terms. The maximum term for a Veterans' Administration guaranteed loan is 40 years if secured by a mortgage on the farm or 10 years if unsecured or secured by a chattel mortgage on the borrower's machinery or livestock. At present, veterans who obtain loans guaranteed under this title pay 4 percent interest.

In the event that the veteran fails to meet his obligations to the lender, the Veterans' Administration, as guarantor, pays the amount of its guaranty to the lender. Any deficiency remaining after the sale of the security is, until discharged or waived, owed by the veteran to the Federal Government.

In addition to the guaranteed loans, the Veterans' Administration manages an insured loan program. This program is used by some lenders instead of the guaranty plan. In this case neither the lender nor the veteran pays an insurance premium. The interest rate on these insured loans may not exceed 5.7 percent.

[2] The Farmers Home Administration also has responsibility for administering certain provisions of Title V of the Housing Act of 1949. Title V authorizes Government loans to help eligible farm families construct, improve, repair, or replace houses and other farm buildings. To be eligible for a loan, a farm family must be unable to get needed credit for housing improvements from other sources. Loans can be made only to farm owners. These loans carry 4 percent interest. They are repayable in a maximum of 33 years. The act also authorizes a limited number of grants to eligible owner-operator farm families to correct housing defects that are dangerous to the health or safety of the farm family or the community.

The Supplemental Appropriation Act of 1950 (Public Law 358, 81st Congress, 1st Session; H. R. 6008) provides funds for carrying out these and other provisions of Title V of the Housing Act.

Conditions Favored by Lenders

Lending agencies are more likely to approve a family's application for a housing-improvement loan if the family has a productive farm. Since a good farm with an improved house will bring a better price on the market than a good farm with an unimproved house, the improvements made on the house add to the value of the lender's security.

Experience has shown, however, that the resale value of the farm does not always increase by the amount actually spent on the house. This is especially true if the improvements have been made during a period of high prices and the farm is sold in a period of lower prices.

Lenders serving families in the less productive farming areas are more likely to take favorable action on an application for a housing-improvement loan if the farm is located close enough to a population center to make it possible for the family to have some nonfarm employment. Another point to be noted is that lenders are more inclined to approve an application for an improvement loan if it is to be used to finance housing improvements that are in line with generally accepted standards in the community. In the event the lender has to accept the property in payment of his loan, he is likely to find that a farm with a dwelling far above the level prevalent in the community is harder to sell.

Finally, lenders favor applications for housing-improvement loans from families that are financially able to carry the debt. The family that has a considerable equity in its farm and has few or no other credit obligations is more likely to have favorable action on its application for a housing-improvement loan than a family that already has a heavy debt load. The best recommendation an applicant for a loan can provide is a record of prompt payment of past debts.

TEN QUESTIONS TO CONSIDER WHEN PLANNING FOR CREDIT

Can the family afford to go in debt?

Before this question can be answered the family will need to make a careful analysis of its assets and liabilities. Such a study will help the family to get a clear picture of its financial situation and to determine whether it is getting ahead financially.

After this has been done, the family will want to make an estimate of its probable income during the next few years. The next step is to make an estimate of the annual outlay for regularly recurring items of expense for family living and farm operating, and for installments on the farm-mortgage loan, insurance premiums, and other savings and investments. An analysis of these figures will indicate whether the probable income will be adequate to take care of all these items and provide a balance with which to pay installments on a loan for housing improvements or for a new house as they come due.

Is it advisable to borrow to finance the purchase of the farm and improvements on the house at the same time?

This question is frequently discussed by farm people and widely different opinions are held. Even though the financing could be arranged, some families are strongly opposed to the idea of financing any housing improvements with credit until the farm-mortgage debt has been paid. Other families are of the opinion that it is unwise to use credit to finance more expensive improvements at the same time that they are paying off the debt on their farm, but that it is all right to use credit for less expensive improvements. These latter might be such articles as a mechanical refrigerator, a power washing machine, or an electric or gas range.

Still other families argue that if conditions are favorable and a satisfactory type of loan contract can be obtained, it is a sound procedure to obtain a loan for housing improvements at the same time that they obtain credit to purchase the farm and from the same lender. Families adopting this plan point out the advantages of living in an improved house from the start.

Is this the best time to make improvements?

Even though the family has decided to use borrowed funds for housing improvements, a number of other matters must be considered before applying for a loan. One is the availability of electricity.

Many of the housing improvements farm families make are dependent on or related to the availability of electricity from a central power station. Some families not yet served with electricity prefer to wait until electric service becomes available to start their housing-improvement program. Others wire their houses and install water pipes and plumbing equipment so that they will have the use of electricity and other modern facilities with a minimum of delay as soon as electric service is obtained.

Another point that needs to be considered is the availability of building materials. If materials of the desired quantity and quality cannot be purchased it probably would be advisable for the family to postpone starting the work until these materials are available. For example, if the only lumber in stock is green, it would be better to wait until seasoned lumber can be obtained.

Along with the supply and quality of materials there is the further question of price. The family will do well to get the opinion of qualified persons as to the trend of prices for construction materials. If the evidence indicates that prices are likely to rise in the near future it may be advisable to place the order promptly, even though building operations cannot be begun until some time later. On the other hand, if it seems likely that prices will decline within a reasonable period, it may be wise to postpone operations until prices have reached a lower level.

Skilled workmen are needed for many housing-improvement jobs. Often they are difficult to find in a rural community. Under these circumstances the family may be well advised to wait until such workers can be hired. Wage rates also need to be considered, both the existing rates and the probable trend.

What improvements are to be made and what will they cost?

Before launching a housing-improvement program, credit-using families will find it to their advantage to make detailed plans of what is to be done. Decisions must be made regarding the various jobs and the best order in which to do them. Estimates must be made of their probable cost.

Jobs to be done.—Families that take time to plan their improvements before the work begins are more likely to get what they want and get it at a lower cost. More time is needed for planning if the job is large, or is to extend over a period of years and is to be financed with borrowed funds.

If the improvements planned involve structural changes in an old house, such as cutting new doors and windows, changing partitions, installing cupboards, or adding a room, it is advisable to make scale drawings. With such drawings the relation of the parts to the whole shows up clearly and may indicate desirable changes in the plans before the actual construction work gets under way. Another advantage of putting the plans on paper is that it helps the family and the hired workers, such as the carpenter, plumber, and electrician, to decide on the best order for doing the work.

In building a new house it is best to have a complete plan with working drawings. If the job is to be contracted for, the contract should indicate the kinds and grades of materials to be used and the quality of workmanship agreed upon.

Cost estimates.—Facts as to cost are essential to any plans for improvements. These facts may be obtained from various sources—the contractor or boss carpenter, the mason, the county extension agents, or a local lumber dealer. If there is a farm-purchasing cooperative in the vicinity that handles building supplies, that may be a good place to go for estimates. The experience of neighbors who have made similar improvements is often helpful.

Estimates of the cost of installing electricity and other modern facilities can be obtained from electricians, plumbers, and heating contractors and from dealers in equipment and building supplies. If family members plan to do part of the work, it is desirable to obtain two estimates of the cost of labor—one, if all the labor is hired; the other, if only part of it is hired.

After the probable cost of various improvements has been determined it is well to increase this estimate by 5 or 10 percent to take care of any mistakes in the original estimate as well as unforeseen expenses. Such additional expenses may result from an increase in the price of construction materials, equipment, or labor, or from costly delays due to bad weather.

Ways of cutting costs.—Many farm families have found ways of reducing out-of-pocket expenses for housing improvement. Several of these ways are discussed below.

Use materials from the family farm.—If improvements to be made call for extensive use of stone, sand, and gravel, it frequently is possible to obtain these materials from the family farm or from that of a neighbor. If the plans call for a considerable amount of lumber, it may be feasible to have it processed from trees grown on the farm or in the neighborhood. Since lumber represents from 35 to 40 precent of the cost of materials for the average frame house, the savings through the use of the farm-furnished product are often considerable even after paying the cost of having the lumber processed. Sometimes it is possible to use second-hand lumber from dismantled farm buildings.

Shop around to get the best values.—Before placing an order for materials and equipment, the first thing for the family to do is to make an estimate of what is needed. Next, it is well for the family to take time to compare merchandise offered and prices quoted by several dealers in one or more towns. Considerable variation is often found in quality and in prices quoted on the same or similar articles in different market outlets. Even when the price tags on identical articles in two different stores are the same, one of the two merchants may offer a discount of 3 to 5 percent for cash. On an article costing several hundred dollars, such a discount represents a sizable saving.

Some families are able to purchase second-hand plumbing and heating equipment, refrigerators, ranges, lighting fixtures, and other items at greatly reduced prices. Others obtain windows and doors at a bargain from a house that is being torn down.

Use farm equipment and family labor for some jobs.—By using the farm tractor, truck, team and wagon, the electric power saw, and the power shovel in construction work and in the hauling, farm families can reduce out-of-pocket expenses. Family members often do such jobs as hauling the supplies, excavating,

pouring cement, rough carpentry, and painting during periods of slack employment on the farm.

Since labor cost (on site) accounts for 35 to 45 percent of the cost of the average frame dwelling it is easy to see that total cost will be greatly reduced by having even a small part of the labor contributed by the farm family or by neighbors with whom the family exchanges work. Whether it is feasible to use family labor or that of other unpaid workers for any or all phases of construction depends on the skill of these workers and the return that could be obtained for their labor in other work.

Employ competent carpenters and mechanics to do the work requiring special skills.—When the job to be done calls for special skills, it is well to hire competent workmen. These workmen often charge no more than those who are less skilled. Because they know how to proceed they waste less time and thus are able to do the job in a shorter time. Because of their greater skill, the completed product is of higher quality and can be maintained in good condition at less cost.

Consider limiting the number of improvements made at one time.—In modernizing old houses some credit-using families limit the improvements made in any one year to those that can be financed with a loan of a few hundred dollars. After this debt is repaid another small loan is obtained and further improvements are made. However, families that follow this practice may find that their improvements actually cost them more in the end than if they had obtained a larger loan at the outset and made all the improvements at one time.

Is it advisable to finance all improvements with a single cash loan?

The family that is using credit to finance several improvements, all to be made at the same time, will do well to obtain a cash loan to cover the cost of all items. Some families finance the wiring of the house with a cash loan, purchase the heating system on open account, and buy the refrigerator on the installment plan. They not only have the trouble of making payments to three different creditors, but their credit actually may cost them more.

Will a short-term or a long-term loan be more satisfactory?

After deciding on how much to borrow, the credit-using family must decide whether to apply for a short-term or a long-term loan. A short-term loan probably will be better for the family that does not need to borrow more than a few hundred dollars and is able to repay its loan in a few years. The shorter the term, of course, the less the amount that must be paid out in interest. In most cases, short-term credit is used to finance the less expensive improvements such as the installation of electricity, the purchase of a refrigerator or an electric or gas range, and such materials as insulating board, roofing, and siding.

Ordinarily, a short-term loan will not meet the needs of the family that wants to borrow money for extensive remodeling of an old house or the building of a new one. Such a family may need a loan of $1,000 or more. In such cases a long-term loan may be better.

What kind of a repayment plan will be most satisfactory?

Each credit-using family wants a repayment plan that takes into account the family's special needs. Several types of plans are outlined here.

Amortized loans.—Many lending agencies now make what is known as the amortized loan. With this, the family agrees to repay its debt on the installment plan. Usually interest and an installment on the principal are combined in a single payment at the end of a year, 6 months, 3 months, or 1 month, depending on the arrangements between lender and borrower. As the family makes each payment, the amount it owes on the principal becomes smaller.

Most of the amortized loans to families are repaid on the level-payment basis so that the amount due on the dates agreed upon is the same each time. For the first few payments, interest payments make up the larger proportion of the installment; later on, payments on the principal make up the larger proportion of the installment. The last few payments consist almost entirely of principal. (See table 1 and fig. 1, pp. 8 and 9.)

Another type of amortized loan sometimes used calls for a fixed payment on the principal at each repayment period plus the interest due at the end of that period. This is known as the level-principal-payment plan.

For the first several payment periods the payments are larger than with loans amortized on the level-payment plan; later on, the payments are smaller. (See table 2 and fig. 2, pp. 10 and 11.) Many families have had experience with one or the other type of amortized loan, since farm-mortgage loans are frequently repaid on the amortized plan.

Loans of $300 to $500 are sometimes set up on the amortized plan as well as loans of $1,000 or more. The smaller loans are usually amortized in 3 to 5 years whereas the larger loans may run for a longer period. The length of the amortization period will probably be determined in part by the lender. Lenders are likely to favor a limited repayment period for improvement loans on old houses. They frequently are willing to make a 10-year loan to a family for the purpose of financing the remodeling of a 50-year-old house, but they may be unwilling to make a 25-year loan on the same property.

Straight loans.—There are several types of straight loans. Practically all provide for making the

interest payments at regular intervals, usually annually. Plans for repaying the principal vary.

The terms under which some straight loans are made include no provision for repayment of any part of the principal until the end of the period for which the note is drawn. At that time the entire amount is due.

Other straight loans are made with the provision that one-half of the loan must be repaid at the end of a specified period, and the balance at the end of the term for which the note is drawn. Thus, on a 10-year loan, the terms may provide that half of the loan is to be repaid at the end of 5 years and the balance at the end of 10 years.

Some families prefer a straight loan because during the years that they have only the interest to pay they have the use of their surplus funds for the children's education, new farm machinery, or for further improvements for the farm and home.

Other families consider a straight loan for major housing improvements less satisfactory than an amortized loan. One reason they may decide against a straight loan is that more money has to be paid out in interest than for an amortized loan. On a straight loan with no provision for repayment before the end of the term for which the note is drawn, interest must be paid on the full amount borrowed for the entire length of the term of the loan. Thus, on a 15-year straight loan of $1,000 at 4 percent, the total interest charges would be $600. On a 15-year amortized loan for $1,000 at 4 percent, to be repaid in 30 equal semiannual installments, the total interest charges would be $326, a difference of $274.

Another reason some families object to a straight loan is that it is more difficult to accumulate the money needed to retire a debt all at one time than it is to retire it in installments. Another disadvantage of the straight loan is that in the event that the borrowing family is unable to repay the loan when due and a new note must be drawn, it may be necessary to have the property pledged as security reappraised. This will be an additional expense to the borrower. If there has been an increase in interest rates the borrower may have to pay a higher rate of interest on the new note.

However, whether to get an amortized or a straight loan is a question that must be decided for each particular case. Each family's situation is different; therefore a repayment plan that is ideal for one family may be quite unsatisfactory for another.

What security will be required?

Long-term loans.—Most lenders making long-term loans to owner-operators for the construction of a new house or for extensive improvements on an old one require a mortgage on the farm or other real estate as security for the loan. If the farm is already mortgaged the family would do well to try to get an increase in the existing mortgage rather than to give a second mortgage.

The family that has a good repayment record on its long-term amortized loan probably will have no difficulty in arranging for an increase in the original farm-mortgage loan. Some lenders will be willing to make the new loan at the same interest rate as the old one. Other lenders may require the borrower to sign a separate note for the increased amount borrowed and pay a higher rate of interest, but will permit him to secure both notes with one mortgage. The terms agreed on for repaying such a debt frequently provide for amortizing it over a 10-, 15-, or 25-year period.

Short-term loans.—Practices vary among lenders as to the security required for short-term loans to farm families. Some lenders require a chattel mortgage as collateral to secure a short-term loan. This mortgage may be placed on the livestock or on some of the farmer's productive equipment. Other lenders make their loans with no other security than the borrower's note or the endorsement of a friend.

What will the loan cost?

Interest.—Interest is the chief item of cost in a loan. With Government-sponsored lending agencies the interest rate is regulated by law. Usury laws set an upper limit for other lenders, but competitive and other factors operate to keep rates below this upper limit.

In the same trading area some lenders may charge lower rates than others. Even with the same lender the rate may vary with different borrowers, depending upon such considerations as size of loan and length of term, the credit standing of the borrower, and the security offered. The rate on a larger loan usually is less than on a small one; the rate on a long-term loan secured by a real estate mortgage usually is less than that on an unsecured short-term loan.

For the country as a whole, the average interest rate on farm-mortgage loans recorded during March 1947 was as follows:

Credit agency:	*Interest rate (percent)*
Commercial banks	4.9
Life insurance companies	4.2
Individuals	4.5
Federal land banks	4.1
Miscellaneous	4.1

Before entering into a loan contract, families will find it to their advantage to get estimates of interest rates and other terms and conditions from more than one lender. For the same loan, running for the same term of years, on the security of the same piece of property, there may be a variation of from 1 to 2 percent in the interest rate quoted to a family by different lenders. Over a period of years this difference is important.

At 5 percent the annual interest on a loan for $1,000 would be $50; at 4 percent it would be $40, an annual saving of $10. If the loan runs for 10 years and no payment is made on the principal during that time the total saving in interest would be $100.

A family that has already established its credit with a lending agency may find that it can get a lower interest rate there than from another lender with whom it has had no previous dealings.

Other charges.—In addition to interest the borrower may have other expenses in connection with his loan. They include recorder's fees for both short- and long-term loans, title clearance expenses, charges for bringing the abstract of title up to date, appraiser's fees, and commissions to lenders for special services in obtaining the loan. Some of these charges, such as recording fees, may be fixed by law. Others, such as commissions, are usually fixed in accordance with local customs or commercial agreements. The borrower has to pay the standard charge. The family that obtains its housing-improvement loan from the lender who holds the farm mortgage probably will be able to effect a savings in some of these charges.

How much more will it cost to live in the improved house?

It costs more to live in a house with modern facilities than in an unimproved house. A central heating system probably will burn more fuel than a

TABLE 1.—*Loan amortization schedule, level-payment plan*[1]

[Principal, $1,000. Rate, 4 percent. 20-year term. Semiannual installment, $37. Final installment, $10.17]

Year due	Payment No.	Interest	Payment on principal	Date paid	Unpaid balance
19—	1	$20.00	$17.00		$983.00
19—	2	19.66	17.34		965.66
19—	3	19.31	17.69		947.97
19—	4	18.96	18.04		929.93
19—	5	18.60	18.40		911.53
19—	6	18.23	18.77		892.76
19—	7	17.86	19.14		873.62
19—	8	17.47	19.53		854.09
19—	9	17.08	19.92		834.17
19—	10	16.68	20.32		813.85
19—	11	16.28	20.72		793.13
19—	12	15.86	21.14		771.99
19—	13	15.44	21.56		750.43
19—	14	15.01	21.99		728.44
19—	15	14.57	22.43		706.01
19—	16	14.12	22.88		683.13
19—	17	13.66	23.34		659.79
19—	18	13.20	23.80		635.99
19—	19	12.72	24.28		611.71
19—	20	12.23	24.77		586.94
19—	21	11.74	25.26		561.68
19—	22	11.24	25.76		535.92
19—	23	10.72	26.28		509.64
19—	24	10.19	26.81		482.83
19—	25	9.65	27.35		455.48
19—	26	9.11	27.89		427.59
19—	27	8.56	28.44		399.15
19—	28	7.98	29.02		370.13
19—	29	7.40	29.60		340.53
19—	30	6.81	30.19		310.34
19—	31	6.21	30.79		279.55
19—	32	5.59	31.41		248.14
19—	33	4.96	32.04		216.10
19—	34	4.33	32.67		183.43
19—	35	3.66	33.34		150.09
19—	36	3.01	33.99		116.10
19—	37	2.32	34.68		81.42
19—	38	1.63	35.37		46.05
19—	39	.92	36.08		9.97
19—	40	.20	9.97		

[1] Figures supplied by Farm Credit Administration.

space heater. Electricity for lighting is likely to cost more than kerosene. If electricity is also used for cooking, to operate the refrigerator and the pump, and to heat the water for kitchen and bath, the monthly bill may be an item that needs special attention in the family budget.

Some allowance also needs to be made for servicing charges on the range, refrigerator, pump, and other facilities and appliances. Real estate taxes on the farm property may increase slightly because of higher valuation. The premium on the fire and windstorm insurance may be somewhat higher.

With increased outlay for all of these items, family living expenses are likely to be higher than before the house was modernized. This is further reason why it is important for the family that is financing these improvements with credit to get a loan contract in which repayment is extended over a period of years and in which the fixed charges for annual repayment of principal and interest are kept low.

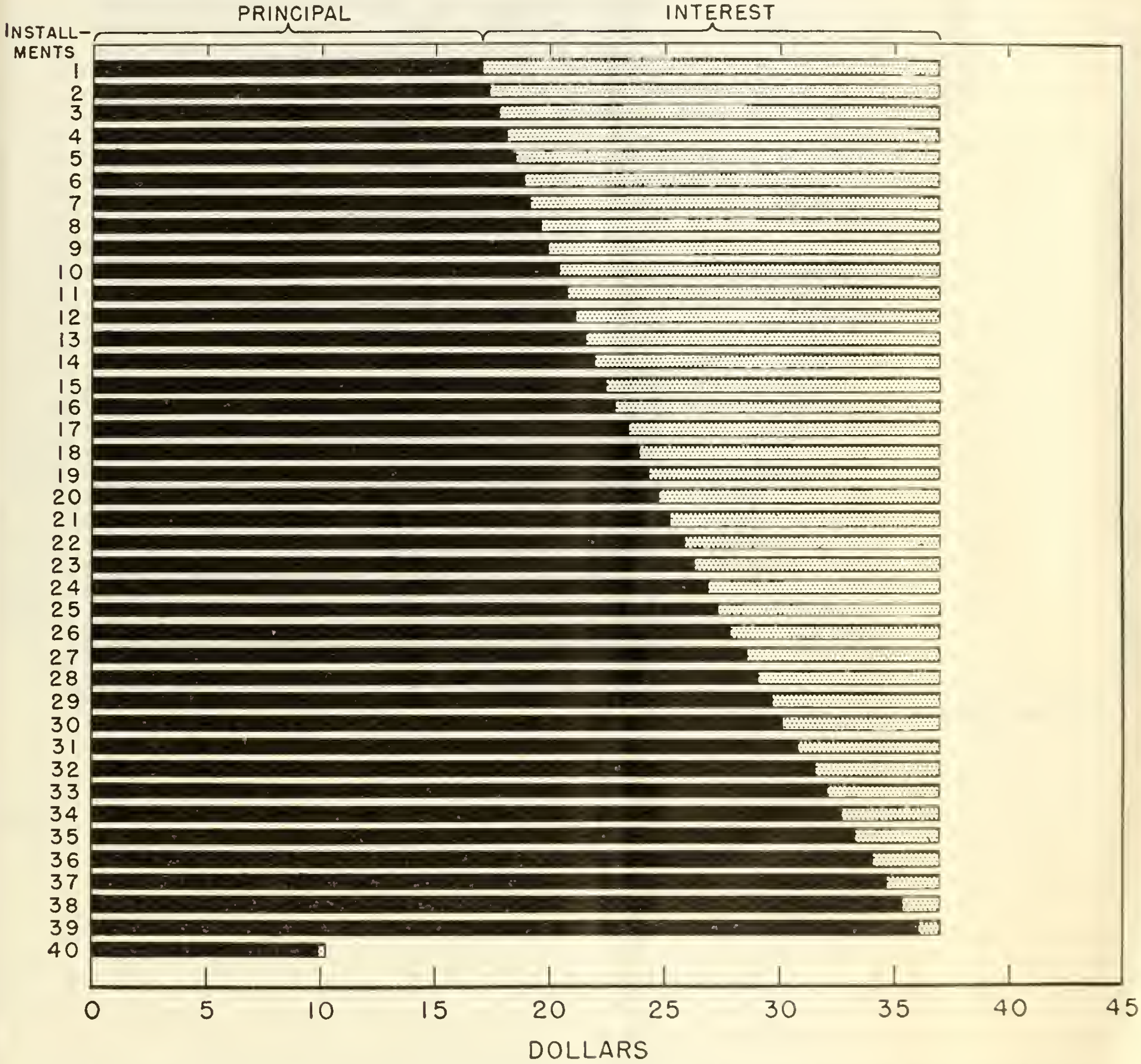

Figure 1.—Level-payment plan for repayment of semiannual principal and interest on a $1,000, 4-percent, 20-year loan.

TABLE 2.—*Loan amortization schedule, level-principal-payment plan* [1]

[Principal, $1,000. Rate, 4 percent. 20-year term. Installments paid semiannually. Final installment, $25.50]

Year due	Payment No.	Total installment	Interest	Payment on principal	Date paid	Unpaid balance
19—	1	$45.00	$20.00	$25.00		$975.00
19—	2	44.50	19.50	25.00		950.00
19—	3	44.00	19.00	25.00		925.00
19—	4	43.50	18.50	25.00		900.00
19—	5	43.00	18.00	25.00		875.00
19—	6	42.50	17.50	25.00		850.00
19—	7	42.00	17.00	25.00		825.00
19—	8	41.50	16.50	25.00		800.00
19—	9	41.00	16.00	25.00		775.00
19—	10	40.50	15.50	25.00		750.00
19—	11	40.00	15.00	25.00		725.00
19—	12	39.50	14.50	25.00		700.00
19—	13	39.00	14.00	25.00		675.00
19—	14	38.50	13.50	25.00		650.00
19—	15	38.00	13.00	25.00		625.00
19—	16	37.50	12.50	25.00		600.00
19—	17	37.00	12.00	25.00		575.00
19—	18	36.50	11.50	25.00		550.00
19—	19	36.00	11.00	25.00		525.00
19—	20	35.50	10.50	25.00		500.00
19—	21	35.00	10.00	25.00		475.00
19—	22	34.50	9.50	25.00		450.00
19—	23	34.00	9.00	25.00		425.00
19—	24	33.50	8.50	25.00		400.00
19—	25	33.00	8.00	25.00		375.00
19—	26	32.50	7.50	25.00		350.00
19—	27	32.00	7.00	25.00		325.00
19—	28	31.50	6.50	25.00		300.00
19—	29	31.00	6.00	25.00		275.00
19—	30	30.50	5.50	25.00		250.00
19—	31	30.00	5.00	25.00		225.00
19—	32	29.50	4.50	25.00		200.00
19—	33	29.00	4.00	25.00		175.00
19—	34	28.50	3.50	25.00		150.00
19—	35	28.00	3.00	25.00		125.00
19—	36	27.50	2.50	25.00		100.00
19—	37	27.00	2.00	25.00		75.00
19—	38	26.50	1.50	25.00		50.00
19—	39	26.00	1.00	25.00		25.00
19—	40	25.50	.50	25.00		

[1] Figures supplied by Farm Credit Administration.

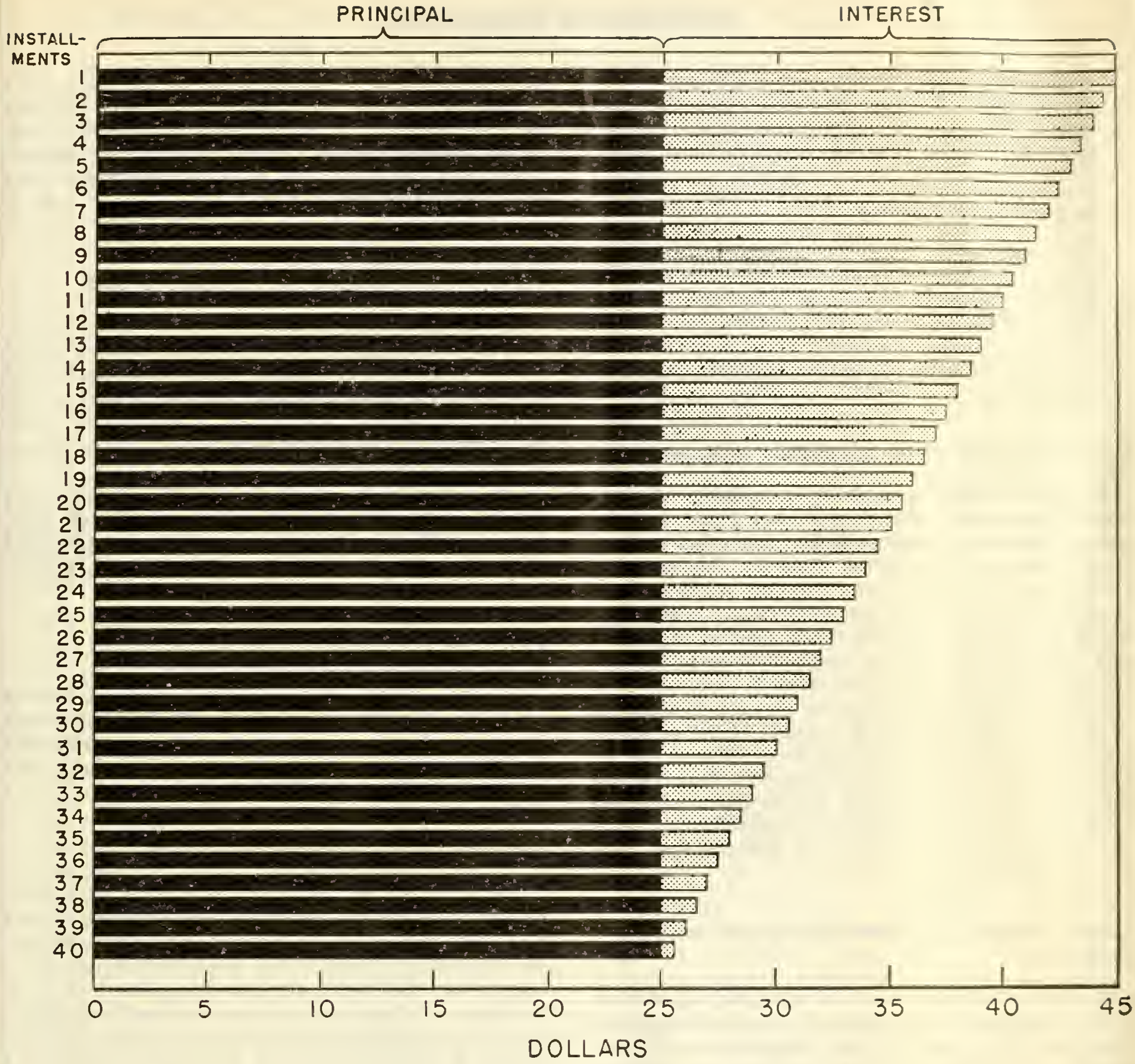

Figure 2.—Level-principal-payment plan for repayment of semiannual principal and interest on a $1,000, 4-percent, 20-year loan.

In making housing improvements all families will find it to their advantage to follow sound business practices. This is especially important for families using credit. A few recommended practices follow.

Have credit terms in writing

The family needs to have a written record of such matters as the exact amount of credit extended, the credit charges, the length of the term, and the plan agreed upon for repaying the principal sum. It is well also for the family to keep a record of the dates when payments were made, the amounts paid, and the balance due.

Get a budgeted loan for construction expenses

Families building new houses or making extensive improvements on old houses and financing the construction with credit will find it to their advantage to obtain a budgeted loan for this purpose. Under such a plan the total amount of loan funds needed to finance the entire undertaking is arranged for at the outset, but the funds needed to finance each separate job are not credited to the borrower's account until the date specified in the contract. Interest is computed separately on each installment of the loan from the time it is made available to the borrower. Thus the borrower pays interest on the loan only while he is using the credit. But because the loan has been arranged for at the outset, the funds are available as needed—to pay the carpenter, the plumber, and the lumber dealer when they present their bills.

Specify in writing all materials to be used and jobs to be done

Families will find it to their advantage to have a written agreement or contract in negotiating with individuals or firms for the installation of electricity, for a water supply and sewage disposal system, for insulating the roof, for providing other materials of specified quantity and quality, or for the construction of the house itself. In such a contract the details of the jobs to be done and the grade of materials to be used should be set forth, as well as the terms of payment.

The responsibilities of the seller should be clearly stated. For example, a contract for the sale of a central heating system should include such particulars as the type of system to be installed, the specified fuel capacity, the date the installation is to be completed, the price, and the terms of sale.

The responsibility of the buyer should also be set forth—to pay cash upon delivery if this is what is agreed upon, or to make a down payment of a certain proportion of the total figure upon delivery and the balance in installments on specific dates or at specific stages in the construction process. Thus both the buyer and the seller will know what is expected of them and misunderstandings will be avoided.

Have all bills itemized and receipted as paid

Misunderstandings are avoided, and record-keeping is simplified if the bills submitted to the family provide an itemized list of materials used and the time (hours or days) actually spent on the job by workmen. The detail in which this needs to be done will be determined in part by the nature of the job contracted for.

After bills have been paid and receipted they should be placed in a convenient file where they are readily available when needed. They will be useful as proof that the family has used the loan for the purpose stated in the application.

Make payments on loans when due

Families that have established a reputation for promptness in meeting their credit obligations find it easier to borrow money. Furthermore, they may be able to get more favorable terms than those that are careless about these matters.

Test improvements before final payment

Families that are building a new house or making major improvements on an old one are advised that their contract with the builder should provide for withholding payment of the final installment of the contractor's bill until the job has passed final inspection. If the improvements include the installation of a central heating or a central plumbing system, it may be desirable to have the contract provide a withholdal of the final payment until the family has occupied the house for a time and has been able to test the improvements through use.

Carry adequate insurance

In order to protect their equity, lending agencies usually require their borrowers to carry fire and other hazard insurance on property offered as security for a loan. It is to the family's interest to see that the policy provides additional hazard insurance to protect its own equity in the property. The family may also be advised to take out insurance on the life of the head of the household for a sum equal to the amount of the loan.

HOW MUCH CAN FARM FAMILIES AFFORD TO INVEST IN HOUSING?

In making plans for improving their houses, especially when credit is to be used, farm families may ask for a rule to help them decide how much they can afford to spend for the house. They ask, for example, whether the investment in the house might reasonably be a certain share of the investment in land, service buildings, and farm equipment.

There are many reasons why there is no precise answer to this question. One is the problem of putting a value on the investment in the farm. Should the investment be valued in terms of the price paid for the property or in terms of its probable sale value? Neither one provides a satisfactory basis, especially in a period of markedly changing prices. Moreover, farms differ greatly in their requirements for farm buildings and machinery. For some types of farming—dairying for example—it is necessary to invest a considerable sum in buildings; for other types, as grain and cotton, much simpler farm buildings are adequate. Whether the amount invested in the farm business is large or small, the basic housing needs of all families are the same.

Farm families often ask whether the rule-of-thumb method sometimes suggested for city families—two to two and one-half times the annual income for a house—is a safe rule for them to follow in arriving at an estimate of the amount that can safely be invested in a house.

This is not a useful rule for farm families. Even for city families it has limited value. With farm families, income frequently fluctuates widely from year to year. Under these conditions an investment that must be carried over many years cannot be determined on the basis of the income for a single year.

The ability of farm families to provide good housing is closely related to the adequacy of their farms as economic units. The amount that a specific owner-operator farm family can afford to invest in a house depends in the final analysis upon the long-run, income-producing capacity of its farm or the long-run possibilities for dependable nonfarm income in that community. A productive farm can usually support a good house, an unproductive farm cannot. The higher the farm income over the years the better the house it is possible for the family to have.

Many other considerations enter into the farm family's decision as to the amount it can afford to invest in its house. The farmhouse is frequently the center for activities connected with the farm business. Often poultry is dressed and eggs are packed in the house; vegetables are bunched and crates of berries and other small fruits are assembled there. Conferences with prospective buyers of farm products are sometimes held in the farmhouse. It is in the house, too, that financial plans are made and records are kept. Families may decide to invest in certain housing improvements because these improvements will make the house a more efficient business unit.

A modern farmhouse may contribute to the income in other ways. Farm women often carry on some income-producing enterprise of their own. Many of them report that after their houses have been modernized they are able to do their housework in less time and with less fatigue. This means that they are able to devote more time and energy to the care of the poultry flock or the processing of food to sell on the market.

A family's ability to save is another point to be considered in deciding how much can be invested in housing, especially if credit is to be used. Families vary so greatly in this respect that no generalizations are possible. Getting out of debt is very important to some families and they find ways to save the money needed to pay installments on a housing-improvement loan in bad seasons as well as good. Other families with equally good intentions find it difficult if not impossible to meet their credit obligations. Such families may be well advised to proceed very cautiously with their housing improvements.

In making so important a decision as the amount to be invested in a farmhouse, the farm family should realize that economic issues are not the only ones to be considered. Families are not long content with houses that do no more than meet their basic needs for shelter. Nor are they content to stop when they have made the minimum improvements suggested as necessary to enhance the value of the farm. Families look upon their dwellings as something to enjoy as they enjoy their automobiles, their clothes, and appetizing foods. They justify the expenses involved in a good house, in part because it contributes to the family's income and to the value of the farm property, and in part because it adds to the family's pleasure.

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